VII. Globalization and Naval Forward Presence

VII.1 Introduction

When this study was undertaken, one objective was to integrate the quantitative findings of our analysis with the more qualitative approach to globalization undertaken by the National Defense University (NDU). As it turns out, the NDU study will not be released until the fall 2000. We have not been able to obtain advanced copies or preliminary results. Still scattered accounts (Dicks, "Navy Leaders Call for Boost in Budget Topline," Defense Daily, June 21, 2000) suggest that the findings of that effort are consistent with the ones presented here. In particular, a major conclusion of that study apparently will be that "the presence of Navy ships and personnel worldwide has a positive impact on trade and jobs at home."

VII.2 Components of Globalization

As usually defined, "globalization" means the process of making something worldwide in scope and application. It most commonly refers to the stunning increase in the number and variety of transnational transactions. The process of adapting to global conditions requires adjustments on the part of both producers and consumers. Specifically, globalization refers to the worldwide convergence of supply and demand. This convergence takes many forms:

- Trade (goods, services)
- Finance (banking, investment, foreign exchange, capital movements)
- Communication (information, education, technology)
- Governance (institutions, education, technology)
- Culture (art, music, entertainment) and
- Work and leisure (labor, migration, tourism).

From a purely economic perspective, there are five main trends of importance. The first trend is the upsurge of trade and changing trade linkages. During the 1985-2000 period, supported by the proliferation of multilateral and regional trade initiatives, the ratio of world trade to GDP rose approximately three times faster than in the ten years prior and twice as fast as in the 1960s. Developing countries increased their share of world trade from 23 percent in 1985 to over 30 percent in 2000. They also deepened and diversified trade linkages. Inter-developing country trade increased from 31 percent of total developing country trade in 1985 to over 40 percent by 2000. Between 1985 and 2000 the share of manufactured products in developing countries' exports increased from 47 percent to around 85 percent. A significant share of world trade is intra-firm and stimulated by FDI (foreign direct investment) as firms seek to reduce costs and tap new markets.

The second trend is the integration of world capital markets. Developing countries are becoming increasingly integrated into the global financial system, following the liberalization of financial markets of recipient and source countries. Often with the aid of the International Monetary Fund (IMF), many developing countries have removed restrictions on payments for current account transactions, and lifted controls on cross-border financial flows, especially controls on foreign inflows. The good growth performance of some developing countries has contributed to make emerging markets more attractive to investors from advanced countries wishing to diversify their portfolios.

The third trend is the increased importance of private flows and foreign direct investment (FDI). The magnitude of private flows now overwhelms official financing. Capital inflows more than doubled in relation to developing country GDP between the early 1980s and 2000, with private capital flows rising from an annual 0.5 to 1.0 percent of developing country GDP to over 2 percent by 2000. Contributing to the rapid growth of FDI to developing countries in recent years has been the adoption of strong outward-oriented policies, including substantial improvements in their investment codes, embodying a shift from sovereign discretion to a free flow of FDI. FDI however has flowed massively towards only a few developing countries experiencing fast economic growth: for example during 1990-96 Asian countries received twice as much in percent of their GDP than African countries. Two thirds of all FDI during the last decade went to just eight developing countries, and half received almost none.

The fourth trend is the advances in telecommunications and transport. The main factor behind globalization has been the increased ease and falling cost of communications—including transportation. The cost of phone calls has fallen by a factor of sixty since 1930 and air-passenger miles per capita have increased 15 times in the last 20 years. The advent of faxes and a global computer network has brought fundamental changes in the ways businesses and governments operate.

The fifth trend is the changes in the movement of labor. As the world becomes more interconnected, flows of people across national borders have increased, though they remain small, contributing to ease labor bottlenecks and transfer managerial know-how. The largest flows are between developing countries, but flows from developing to industrial countries have accelerated over the past two decades. In the future one can expect pressures for increased migration from developing countries, whereas developed countries will lower their demand for immigrant labor.

Globalization is spreading at an uneven pace, but wherever it develops, it has important security implications. Clearly, in an economic sense it blurs national boundaries. Whether and to what extent it erodes the power of nation-states, even as it extends their sovereignty into new areas, is a controversial issue with strong arguments made pro and con. However, it clearly changes regional and international power relationships, shifts the mixture of interests at stake, and redefines long-standing alliances and conflicts. It will greatly influence the shape, content, and legitimacy of the future global security order (Strategic Assessment 1999, National Defense University, p. 19).

During the Cold War, the US consciously pursued its own version of globalization. It sought to integrate and expand the democratic, market-oriented, western or pro-western community of nations, and was not afraid of using military force to achieve the goal of spreading democracy. This community-building strategy encompassed both security and economics. The security component created a Western alliance system anchored in containment, deterrence, and collective defense. The economic component established a cooperative, rules-based trading system that rejected protectionism and lowered trade and investment barriers. Both components encouraged the notion that cooperation serves national interests better than conflict. Both stimulated greater efficiency, which freed up military and economic resources for more productive investment. In the post-Cold War era, this dual policy of expanding economic and security cooperation remains the main US policy instrument for building a just, stable, and prosperous world order (Strategic Assessment 1999, National Defense University, pp 20-22).

It is generally felt that the United States is well positioned to compete in the global economy. Economic globalization is broadly consistent with US international security and foreign policy interests. It:

- Facilitates integration
- Promotes openness
- Encourages institutional reforms
- Increases efficiency
- Accelerates the growth of US Gross Domestic Product (GDP)
- Helps control domestic inflationary forces.

VII.3 Globalization and the Economic Impact of Naval Forward Presence

Within the environment of deepening globalization, naval forward presence gives the US the ability to shape environments through the strategic positioning of people and equipment. The inherent mobility of naval forces provides the ability to rapidly project and concentrate military power worldwide, deterring and, if necessary, defeating aggression. US naval forces receive an increasing share of crisis response missions because forward deployed naval forces will be the only timely option unconstrained by access agreements.

Naval forward presence can be manifested in a number of ways, but the most common is the presence of a carrier battle group in an area of interest such as the Mediterranean Sea or the Persian Gulf. On average, 50 percent of the U.S. Navy's active fleet is underway on any given day, and more than a third is forward deployed.

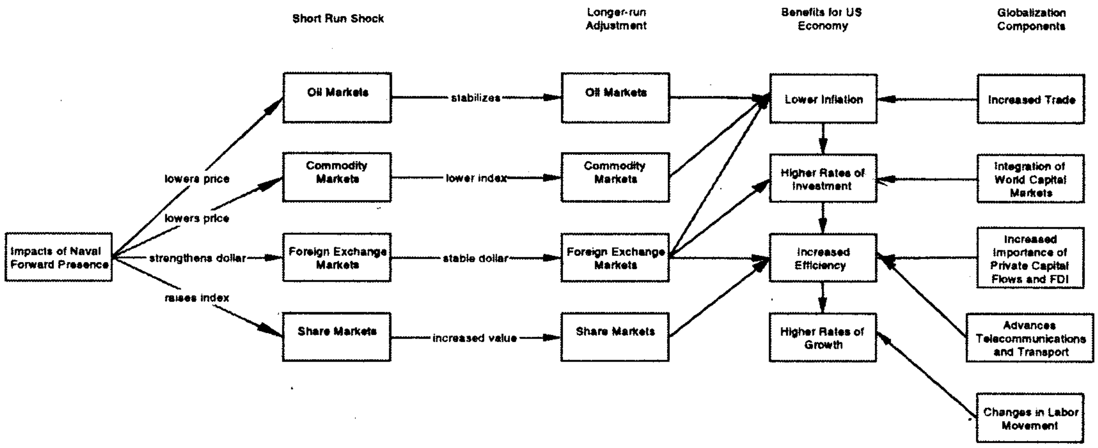
The United States is a maritime nation, and international ocean policy is important to Americans. Today, 95 percent of US foreign trade is transported by sea and it represents 20 percent of the GDP (Strategic Assessment 1999, National Defense University, p. 308). In today's global economy, any interruption in free trade, caused by a military crisis for example, has a negative economic impact, and influences a nation's well being (not only in the troubled region but worldwide). Timely responses by external military forces can stabilize the situation and restore confidence and economic activity. In the economic sense, naval forward presence provides stability and security of free trade, and quick crisis responses.

Economic benefits include the avoidance of losses GDP, reduced unemployment and inflation, expanded industrial production, etc. However, because the role of forward-deployed naval forces is primarily preventive in nature it is difficult to measure the full benefits derived from that activity. In effect, all quantitative measurements of benefits are by nature underestimates because we have no way of assessing the economic costs of the many crisis that were prevented simply because of the presence of naval forces.

With this caveat in mind the findings of the present study of four specific instances of naval forward presence and crisis response suggests that both globalization and naval forward presence complement each other in creating an environment in which the United States economy is able to fare better than would be the case if either or both were absent. These effects and linkages are summarized in Figure 22.

Figure 22

Naval Forward Presence and Globalization: Complementarities and General Impact on the United States Economy

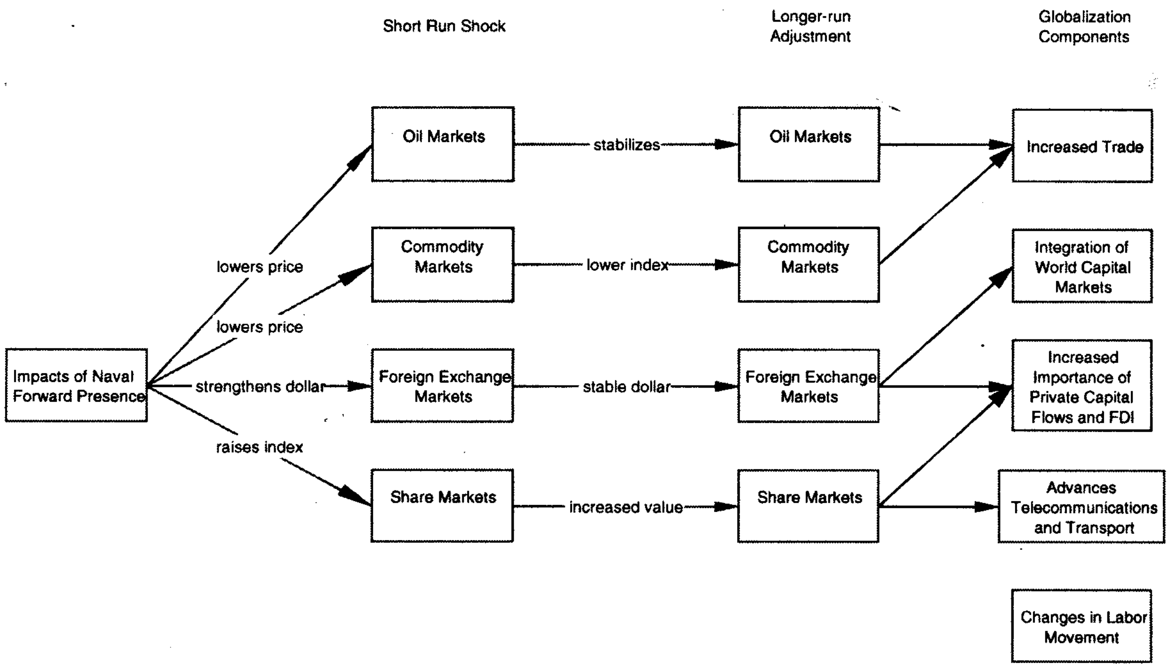


In particular the VAR forecasting models are based on the linkage from oil, exchange rate and share market shifts resulting from naval forward presence and crisis response to increased rates of investment and ultimately higher levels of GDP. While the details, role of exchange rates and share markets, may vary slightly from one case to another the basic mechanism is similar in all cases. On the globalization side of the equation (right hand column in Figure 22), a number of developments in the world market economy tend to reinforce the positive naval forward presence impact on the US economy.

It is also clear that the process of globalization can only proceed in an environment characterized by stable, secure trading conditions, provided in large part by forward deployed naval forces. Specifically (Figure 23), more stable oil prices derived from naval crisis response induce greater trade through reducing some of the risks associated with unexpected increases in transport costs. The stronger more stable dollar associated with naval forward presence aids the development of stronger US share markets (foreign investors avoid much of the exchange risk associated with other markets). The increased value in share markets associated with naval forward presence also increases investment and ultimately economic growth.

Figure 23

Naval Forward Presence and Globalization:
Effect of Naval Forward Presence on the Components of Increased Globalization



While the results of the study suggest that naval forward presence and crisis response have a strong and positive impact on the US economy, some observers have argued that in the future these impacts are likely to be diminished. For example one might argue that oil accounts for a lower share of GDP (energy conservation, alternative fuels) so that the oil shocks that have disrupted the economy in the past are becoming less and less of a threat to prosperity. A corollary is that the so-called new economy is more of a service economy and much less dependent on energy and raw materials. Despite the fact that this is a commonly held view, it is not based on any real hard evidence. Our results suggest a fairly significant oil related impact on the US economy under a series of alternative environments. While the magnitudes of each case vary greatly, there is no apparent trend towards diminished effectiveness of forward deployed naval forces in stabilizing oil markets. Finally, several recent studies avoid the new economy arguments by contending that the recent expansion in the economy is due to a good oil shock (fairly long period of low oil prices).

VII.4 Conclusions

As for the future, it is likely that increased world trade (Figure 24) and increased economic growth associated with globalization will place a growing demand on oil supplies creating the chance of more volatile oil shocks associated with crisis around the world. These developments rather than lower the impact of naval forces will actually enhance the chance of favorable interventions by forward deployed naval forces. Similar arguments can be made for likely changes in the share and foreign exchange markets.

In sum, likely changes in the various facets should strengthen the economic impacts of naval forward presence and crisis response. In turn, the stability provided by naval forward presence should assure continued deepening of the globalization process. This would set up a virtuous circle that would reinforce itself over time.

Figure 24

Naval Forward Presence and Globalization:
Effect of Likely Globalization Trends on the Economic Impacts Associated with Naval Forward Presence